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J. Thomas Greene; Marr, Wilkins & Cannon; Attorneys for Plaintiff-Appellant;

Norman S. Johnson; Attorney for Defendant-Respondent;

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IN THE SUPREME COURT
of the
STATE OF UTAH

UNIVERSITY UTAH

MAY 2 1962

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In the Matter of the Premium Tax
Liability of the SURETY LIFE IN-
SURANCE COMPANY for the
Calendar Year 1959.

No. 193 9570

FILED
BRIEF OF APPELLANT

On writ of Review from the Judgment of the State Tax
Commission of Utah

Hon. Allan M. Lipman, Commissioner
Hon. Orville Gunther, Commissioner
Hon. Arias G. Belnap, Commissioner

J. THOMAS GREENE
Marr, Wilkins & Cannon
920 Continental Bank Building
Salt Lake City 1, Utah
Attorneys for Plaintiff - Appellant

NORMAN S. JOHNSON
State Tax Commission of Utah
State Capital Bldg.
Salt Lake City, Utah
Attorney for Defendant - Respondent

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IN THE SUPREME COURT of the STATE OF UTAH

In the Matter of the Premium Tax
Liability of the SURETY LIFE IN-
SURANCE COMPANY for the
Calendar Year 1959.

} No. 193

BRIEF OF APPELLANT

STATEMENT OF THE KIND OF CASE

This is an action to reverse an administrative ruling by the State Tax Commission of Utah disallowing a deduction on Surety Life Insurance Company's Premium Tax Return for the year 1959. The ruling of the State Tax Commission of Utah is dependent upon correct interpretation of Utah statutes.

DISPOSITION BY STATE TAX COMMISSION OF UTAH

The case was presented to the State Tax Commission of Utah on informal hearing after which an agreed-upon stipulation of facts was entered into by respective counsel. The State Tax Commission of Utah adopted as its

findings the said stipulation of facts and rendered its conclusions of law and final decision adverse to the position of Surety Life Insurance Company on September 29, 1961.

RELIEF SOUGHT ON WRIT OF REVIEW

Appellant seeks an order vacating the decision of the State Tax Commission of Utah and requiring the said Commission to render a new decision allowing the full deduction as computed on appellant's Insurance Premium Tax Return for 1959.

STATEMENT OF FACTS

The findings of fact indicate that Surety Life Insurance Company is a stock legal reserve life insurance corporation duly organized under the laws of the State of Utah, and domiciled in this state. Accordingly, it is a "domestic insurance carrier" within the meaning of that term as referred to herein. The company commenced business in Utah in 1936 and has thereafter fully qualified and complied with the laws of this state and various other states in which it does business. During the year 1959 the company was qualified and doing business in several states. There follows a statement of the nature and volume of such business allocated by states and territories for the year 1959 with an analysis of premiums paid to the company:

	Life	Accident & Health	Total
Arizona	\$ 132,784.00	\$ 106,295.42	\$ 239,079.42
Colorado	50,195.42	80,947.82	131,143.24
Hawaii	8,646.03	5,757.02	14,403.05
Idaho	184,783.01	197,662.06	382,445.07
Montana	103,372.94	96,191.19	199,564.13
Nevada	181,712.40	87,427.60	269,140.00
New Mexico....	25,172.82	20,329.28	45,502.10
Oregon	55,857.66	111,398.74	167,256.40
South Dakota..	42,650.34	28,192.94	70,843.28
Utah	614,350.32	192,481.09	806,831.41
Washington	194,820.25	228,743.23	423,563.48
Wyoming	87,504.15	90,650.77	178,154.92
Misc. States	72,857.50	40,288.74	113,146.24
	<u>\$1,754,706.84</u>	<u>\$1,286,365.90</u>	<u>\$3,041,072.74</u>

During the year 1959 a full and complete examination of the business and affairs of the Surety Life Insurance Company was made pursuant to law. A report on this examination was made as of December 31, 1958, published September 4, 1959. The total cost of the examination paid for in the year 1959 by Surety Life Insurance Company was \$15,946.97. This total may be broken down as follows:

Paid to Harold O. Smith, Examiner in Charge, and other examiners from the State of Utah.....	\$ 3,932.20
Paid to Patrick Coursey, examiner from the State of Colorado.....	3,840.00

Paid to William B. Johnson, examiner from the State of Arizona.....	4,016.88
Paid to L. W. Pfarrer, actuary from the State of Colorado	3,892.13
Printing Expenses	265.76
	<u>\$15,946.97</u>

The Surety Life Insurance Company filed an insurance premium tax return with the State of Utah for the calendar year 1959 in which the amount of tax on total net premiums was accurately computed at \$13,402.95. The company claimed as a credit therefrom the cost of the insurance examination, which exceeded \$13,402.95, leaving no tax due. Thereafter, the Auditing Division of the State Tax Commission of Utah allowed only a partial deduction in the amount of \$4,230.92, and asserted a tax deficiency in the amount of \$9,172.03. This action was upheld by the Commission in its final decision September 29, 1961. The basis for the partial deduction allowance and corresponding tax deficiency was a percentage formula adopted by the Commission, equating premiums paid in Utah with premiums paid in all other states. In computing the deficiency against the Surety Life Insurance Company, the Auditing Division of the State Tax Commission of Utah ascertained that the ratio of premiums collected by the company in Utah relative to the total premiums collected by the company in all states and territories for 1959 was 26.5312 per cent. This percentage was then applied against the \$15,946.97 total cost of examination to the Surety Life Insurance Company so

that the "examination fees allowable" (26.5312%) was computed at \$4,230.92. Then, subtracting the \$4,230.92 from the tax otherwise due on net premiums, the Commission arrived at the alleged \$9,172.03 deficiency.

In considering the factual background relating to this matter, it is necessary to analyze the nature and scope of examinations of domestic insurance carriers in Utah. Such examinations are conducted triennially, and constitute a comprehensive study of the business and affairs of the companies in question. Ordinarily, the examinations are conducted in cooperation with regional or "zone" examinations affecting business done in several states, under the auspices of the National Association of Insurance Commissioners (NAIC). Hence, the comprehensive examinations conducted by the Utah Insurance Commissioner every three years are herein referred to as "triennial-association" examinations. We shall consider the stipulated facts relating to both the "triennial" and "association" features of such examinations generally, and the application of such facts to the Surety Life Insurance Company examination specifically.

(1) Triennial Examinations

The Utah Code provides that:

"The commissioner for the purpose of ascertaining its assets, management, condition and affairs may *fully examine* the affairs, accounts, records, documents and assets of each authorized insurer . . . as often as he deems advisable. Provided, . . . *he shall examine each domestic insurer*

not less frequently than every three years." (Emphasis added.)

31-3-1(1), U.C.A. 1953.

Pursuant to this law, every three years the insurance commissioner of the State of Utah causes to be made a full and complete examination of domestic insurance carriers. This is true whether or not such insurance company does business in states other than Utah, and whether or not the premiums paid into the company are derived wholly from the State of Utah or from other states. Hence the Tax Commission has found that a full examination requires complete consideration of the operations of an insurance company, including analysis of business done outside as well as business done inside the State of Utah (Finding 5(b), R. 28), that whether or not other states join in, such examinations are conducted by examiners who analyze phases of the business of the company independent of and not confined to state lines (Finding 5(d), R. 28), and that premiums paid in Utah bear no relationship to the scope and comprehensiveness of the examination required by the Utah commissioner (Finding 5(e), R. 28). Accordingly, it is observed in the last-named finding that the same scope of examination is required by the Utah commissioner whether one fourth or three fourths of the premiums are paid in Utah.

In connection with such triennial examinations, the Utah insurance commissioner is required to

appoint as his "examiner in charge" a qualified person to ascertain the facts as revealed by the accounts and records of the company and to certify such to the commissioner (31-3-4, U.C.A. 1953). Expenses of these examinations are payable directly by the company being examined to examiners "designated" by the Utah commissioner (31-3-6), U.C.A., 1953), including actuarial assistance if the Utah commissioner regards such as necessary (31-2-5), U.C.A., 1953).

(2) Triennial—"Association" Examinations

The National Association of Insurance Commissioners (NAIC) is an advisory organization to the individual state insurance departments. The organization has gone on record as favoring a co-operative or "zone"-type examination of the books and records of insurance companies where they do substantial business in several states. Accordingly, the country has been organized geographically into six zones, with the State of Utah located within Zone VI along with nine other states. Certain procedures are suggested relative to the conduct of such zone or "association" examinations, as embodied in a "Manual of Association Procedure and Practice" which is incorporated as a part of this record in the Tax Commission's Finding No. 10 (b) (R. 31). It is clear that the manual or any part thereof when used in Utah constitutes only a guide for procedures (Finding 6 (b), R.28, and Finding 8 (a), R. 29). It is in no way binding upon the Utah

commissioner. In fact, the manual clearly recognizes this as well as the over-all responsibility of the insurance commissioner in the domiciliary state for the conduct and supervision of the examination (NAIC Manual, page 8). (The manual also makes clear that assistance in the conduct of the examination shall be supplied by the "home state department" (NAIC Manual, page 5), that all examiners shall be paid in accordance with the statutory provisions of the domiciliary state (NAIC Manual, page 6), that the procedures and methods of the examination shall be determined by the examiner-in-charge (NAIC Manual, page 8) and that the final report of examination shall be adopted by the insurance commissioner of the domiciliary state (NAIC Manual, page 21).)

Utah triennial examinations are conducted as "association" or "convention" examinations or in cooperation with "association" or "convention" examinations where insurance companies do substantial business in other states (Finding No. 6, R. 28). Hence, substantially all of the Utah triennial examinations since enactment of the Utah Insurance code in 1947 have been "association" examinations or have been conducted in cooperation with "association" examinations (Finding No. 6(a), R. 28).

The "association" aspect is injected into Utah triennial examinations at the instance of the Utah Insurance Commissioner. He requests, through the office of the executive secretary of the National

Association of Insurance Commissioners, that an "association" examination be called and that examiners from the states in which the insurance company does business outside of Utah be appointed to cooperate in the examination (Finding 7 (a), R. 29). Ordinarily, in the usual course of things, designated insurance commissioners of states within zones wherein the insurance company does business voluntarily choose to participate in an examination which affects an insurance company doing substantial business in such state. However, there is nothing in the NAIC setup which requires or indeed which could require, such participation. Also, if other states refuse to participate, there is no way in which the Utah commissioner could compel their participation. However, in most instances there is zone participation which results in the tentative appointment of examiners "representing" areas outside Utah. The actual participation of such examiners is subject to the approval of the Utah Insurance commissioner and in all events such examiners act under his direction and under the direction of his "examiner in charge." Hence the Tax Commission has found as to triennial-"association" examinations that the Utah commissioner supplies assistance and supervises the entire examination (Finding 7 (b), R. 29), that actuarial assistance is obtained directly by the Utah insurance commissioner (Finding 7 (c), R. 29), and that an "examiner in charge" is directly appointed by the Utah commissioner

to take charge of the examination (Finding 7 (d), R. 29). As to the report of the examination, which is based upon an analysis of the records and books of the company in question and which constitutes the final work product of the examiners, the Tax Commission has found that conferences between the Utah commissioners and all examiners, as well as the company, are contemplated before the report is approved and certified by the Utah commissioner (Finding 8 (b), R. 29). The report is finally approved, certified and adopted by the Utah commissioner (Finding 8 (c), R. 30), and official distribution of the report is authorized by the Utah commissioner only after he has approved it (Finding 8 (d), R. 30).

As a final set of facts, it is well to note that payment of the expenses of all examiners—out of state as well as those directly appointed by the Utah commissioner—can be made only to examiners who have been “designated” by the Utah insurance commissioner, and that for purposes of payment such examiners are regarded as the Utah “commissioner’s examiners” (31-3-6, U.C.A. 1953).

(3) Surety Life Examination

The Tax Commission in its findings concluded that, “The scope of the Surety Life Insurance Company examination and the conduct thereof was in accordance in all respects with the precepts and facts stipulated to be applicable to Utah triennial

examinations generally . . .” (Finding 9 (g), R. 31). It should be noted that all of the findings referred to in this brief are directly applicable to the scope and conduct of the Surety Life examination.

In addition to incorporating as applicable to the Surety Life examination the findings noted in this statement of facts, as well as other findings applicable to triennial examinations generally, the Tax Commission found specifically that the Utah Insurance Commissioner authorized the Surety Life Insurance Company examination to be conducted as of December 31, 1958 as a triennial examination, and requested through the Executive Secretary of the National Association of Insurance Commissioners (NAIC) that an “association” examination be called and that there be cooperative participation by representatives from states outside of Utah in which the company was doing business (Finding 9 (a), R. 30). The findings also indicate the following:

Direction and Supervision

“The examination was conducted under the direction of Utah insurance commissioner, Carl A. Hulbert, personally and through his designated ‘examiner in charge,’ Harold Smith of Wood, Child, Mann & Smith, Salt Lake City.” (Finding 9 (b), R. 30)

Out-of-state Examiners

“The out-of-state examiners from Arizona and Colorado were selected in due course under

the "zone" examination procedures of the NAIC. These examiners were accepted by the Utah insurance commissioner, Carl A. Hulbert and designated by him to participate in the examination here. During the course of the examination, they consulted with and acted under the direction of Mr. Smith as the examiner in charge and worked through the Utah insurance commissioner's office, having conferences there with Carl A. Hulbert, Insurance Commissioner, and Jack F. Nell, Chief Deputy." (Finding 9 (c), R. 30). (See also Finding 6 (c), R. 28 wherein it is stipulated, among other things, that out-of-state examiners "act under the supervision of the Utah Insurance Commissioner.")

Actuary

"An actuary, Lois Pfarrer, was employed under the direct authority of the Utah insurance commissioner to examine all actuarial phases of Surety's business in all states." (Finding 9 (d), R. 30).

Payment of Examiners

"The out-of-state examiners and the actuary submitted bills for payment to the examiner in charge Harold Smith, who weekly submitted such bills to the Surety Life Company for payment." (Finding 9(e), R. 30).

Use of NAIC Manual

"The 'Manual of Association Examination Practice and Procedure' is ordinarily used as a guide for procedures in such examinations and was so used throughout the Surety Life Insurance Company examination." (Finding 8(a), R. 29).

Report of Examination

"The report which was prepared by the Examiner entitled 'Report on Examination, December 31, 1958,' was first submitted to Carl A. Hulbert, Utah Insurance Commissioner, in rough draft form for suggestions and modifications, and after various changes and additions were made at the suggestion of the Utah insurance commissioner's office and consultation through the Utah insurance commissioner's office with the Surety Life Insurance Company, the report was approved, certified and adopted by the Utah insurance commissioner and the original thereof was filed in the office of the Utah insurance commissioner. Thereafter, under the authority of the Utah insurance commissioner, the report was circulated to various other states."

(Finding 9 (f), R. 30, 21). See also Findings 6(b), R. 28, 8(a), R. 29, and 8(b), R. 29.

ARGUMENT

The fundamental question presented to this court is whether the cost of the 1959 Surety Life Insurance Company examination is wholly deductible as an examination "required" by law within the meaning of Utah Code Annotated 31-14-4(3). That statute provides:

"If any insurance company shall have paid . . . any fee for examination *required by this Code* during said year it shall be *entitled to deduction from the tax herein provided for . . . the amount of any such examination fee.*" (Emphasis added.)

POINT I

THE SURETY LIFE INSURANCE COMPANY EXAMINATION WAS "REQUIRED" UNDER UTAH LAW.

The Tax Commission has found that so-called "triennial" examinations of domestic insurance companies are undertaken and assumed by the Utah insurance commissioner every three years "pursuant to law" (Finding 5 (a), R. 27, 28). This requirement of law is directly imposed upon our insurance commissioner by Utah Code Annotated 1953, 31-3-1(1) which provides:

"The commissioner for the purpose of ascertaining its assets, management, condition and affairs may *fully examine* the affairs, accounts, records, documents and assets of each authorized insurer . . . as often as he deems advisable. Provided, . . . *he shall examine each domestic insurer not less frequently than every three years.*" (Emphasis added.)

The following statutory provisions also have a bearing upon the responsibilities imposed by law upon the Utah insurance commissioner relative to the conduct of examinations of insurance companies in this state:

31-2-1 (Cum. Supp.) U.C.A. 1953:

"The insurance department of the State of Utah is charged with the *execution of the laws relating to insurers* doing business in this State." (Emphasis added.)

* * *

31-2-3, U.C.A. 1953:

"It shall be the duty of the commissioner . . . to keep and preserve in form a full record of the proceedings of his office, *including a concise statement of the condition of all insurers reported and examined by him*; . . . and generally to perform

all duties imposed on him by law.” (Emphasis added.)

31-2-5, U.C.A. 1953:

“With the approval of the commission he (the insurance commissioner) may *employ competent persons to make examinations of the conditions and affairs of insurers when necessary as required by law.* . . . Whenever necessary the commissioner with the approval of the commission shall employ a competent actuary to perform the actuarial duties of the department and to assist in or take charge of *the examinations of insurers under the general direction of the commissioner.*” (Emphasis added.)

31-3-4, U.C.A. 1953:

“The commissioner shall make a *full written report* of each examination made by him containing only facts ascertained from the accounts, records, and documents examined and from the sworn testimony of individuals.

“*The report shall be certified by the commissioner or by his examiner in charge of the examination.*” (Emphasis added.)

31-3-6, U.C.A. 1953:

“(1) *Any examination*, or any part of the examination of any person domiciled or having its home offices in the state requiring travel and services outside this state, *shall be made by the commissioner or by examiners designated by him* and shall be at the expense of the person examined.

“(2) The person examined and liable therefor shall pay to the *commissioner’s examiners* upon presentation of itemized statement thereof,

their actual travel expenses, a reasonable living expense allowance, and per diem compensation at the customary rate, incurred on account of the examination.

The *commissioer or his examiners* shall not receive or accept any additional emolument on account of any examination." (Emphasis added.)

Based upon 31-3-1(1), U.C.A. 1953, it is submitted that an examination of domestic insurers is clearly "required" under Utah law every three years. That requirement of law is directly imposed by the said statute upon the Utah Insurance Commissioner, and the additional laws quoted are in harmony with and in furtherance of such statutory duties. It is clear both from the statutes and the Findings of Fact of the Tax Commission that triennial examinations must be comprehensive and complete without regard to state boundaries, premiums paid, business done in other states, or any other factor.

Notwithstanding the Findings of Fact and the above-quoted statutory provisions, the position of the State Tax Commission of Utah would appear to be that Utah law does not *always* "require" a complete and comprehensive examination of domestic insurance carriers. (It is believed that the Tax Commission would agree that the statute *sometimes* requires such a complete and comprehensive examination, i.e., in the situation where an insurance company does not do substantial business in other states, or in the situation where an insurance company does do substantial business in other states but wherein examiners from other states fail to join in the examina-

tion.) The argument appears to be that when the triennial examination is conducted in cooperation with the so-called "association" or "convention" examination, then only a part of the examination is "required" by Utah law. Our statute provides that:

"Regular examinations of any domestic insurer authorized to do business in other states shall be coincident with and as part of the regular convention examination, if any, of the insurer made by or on behalf of the other states."
31-3-1(3), U.C.A. 1953

This statutory provision certainly doesn't excuse the fundamental obligation imposed by law upon the Utah commissioner to "fully examine" domestic insurance carriers every three years. At most it contemplates a cooperative effort. But the mere fact of fortuitous participation in such examinations by other states could not absolve the Utah commissioner from affirmative duties in connection with examinations of domestic insurers. Notwithstanding such participation by examiners from other states, ultimate responsibility would continue to be with the Utah commissioner. In any event, each and every duty in connection with such examinations is retained by our Utah commissioner, whether or not the association feature becomes a factor in the examination.

It should be noted in connection with 31-3-1(3), U.C.A. 1953, that the examination we are dealing with was not an "association" or convention examination "made by or on behalf of the other states." Hence, the

literal wording of the statute does not apply. An “association” examination of a domestic company domiciled in Utah could be instigated by insurance commissions outside of the State of Utah and hence such examination would be “made by or on behalf of the other states.” That simply is not the case relative to the Surety Life examination. The Surety Life examination was authorized by the Utah Insurance Commissioner as a triennial examination, with the request for cooperative participation from other states (Finding 9(a), R. 30).

It is submitted that the ultimate responsibility for the conduct of the entire Surety Life examination, notwithstanding the “association” feature, was with the Utah Insurance Commissioner both as a matter of law and of fact. As to our insurance commissioner’s responsibility as a matter of fact, the following findings of the Tax Commission are particularly pertinent: the examination was authorized by the Utah commissioner (Finding 9a), R. 30); all examiners were designated by and acted under the supervision of the Utah insurance commissioner (Finding 9(c), R. 30); all examiners were paid as designated examiners of the Utah commissioner (Finding 9(e), R. 30); the entire examination was under the supervision and control of the Utah insurance commissioner (Finding 9(b), R. 30); actuarial assistance was obtained directly by the Utah insurance commissioner without any consultation with the NAIC or any other organization or insurance department (Finding 9(d), R. 30); the “examiner in charge” was directly appointed by the Utah insurance commissioner (Finding 9(b), R. 30);

and the final report of the examination was approved, certified and adopted by the Utah insurance commissioner and it was distributed only after it had been approved by the said Utah insurance commissioner (Finding 9(f), R. 30). In addition to these specific factual findings, it is apparent that the concept of ultimate responsibility of the domiciliary state insurance commissioner for the supervision and conduct of "association" examinations is entirely consistent with, and is in fact, contemplated by, the procedures set forth by the National Association of Insurance Commissioners. (N.A.I.C. Manual)

As to the absolute responsibility of the Utah commissioner as a matter of law for the conduct of such triennial examinations, reference should be made to the duties imposed by statute as above quoted, and particularly to the unequivocal language of 31-3-1, U.C.A. 1953. The Utah Supreme Court has specifically taken note of this statutory requirement:

"The insurance commissioner is directed by statute to order an examination 'not less frequently than every three years'."

Utah Farm Bureau Insurance Co. v. State Tax Commission, 9 Utah 2d 421, 427, 347 P.2d 179 (1959).

One way to test the ultimate responsibility of the Utah insurance commissioner regardless of the "association" feature of the examination is to postulate the entirely conceivable state of facts that other states might refuse or fail to join in the Utah examination as requested by the Utah commissioner. It is clear that the Utah com-

missioner nonetheless would be obliged to conduct a full and comprehensive examination *whether or not the examination should become a triennial - "association" examination*. The statute does not contemplate that the responsibility of the Utah commissioner be changeable at the option or conduct of officials in other states. Neither is the responsibility of the Utah commissioner capable of division; that is, it could not be said that the Utah commissioner is responsible for only a part but not all of an examination. It is submitted that the responsibility imposed by law upon the Utah commissioner for the conduct of such examinations is uniform, i.e., applicable whether or not there is an association examination, and complete, i.e., applicable as to the entire scope of the examination.

POINT II

THE FULL COST OF THE EXAMINATION IS DEDUCTIBLE.

The Utah State Tax Commission has recognized the deductibility of a portion of the cost of the examination. Thus, from time to time reference has been made by the Tax Commission to the "Utah portion" of the examination and the exclusion of expenses attributable to "business done in states other than Utah." In its final decision the State Tax Commission decided that only \$4,230.92 of the total examination cost, which was \$15,946.97, was deductible. The basis for this curious division is an equation of premiums paid in Utah with premiums paid in all states in which Surety Life does business. It is submitted that there is no legal justification for denying

the entire deduction. It is also submitted that there is no basis in our law for proration of the deduction in accordance with the "formula" thus created by the Commission.

The statute which permits the deduction of examination expenses is unequivocal. As already noted, it provides for "deduction of any fee for examination required by this Code." 31-14-4(3), U.C.A. We have heretofore considered that the entire Surety Life Insurance examination was "required" by the Code notwithstanding the "association" feature of the examination. We must now consider whether there is basis in Utah law to disallow as a deduction a part of the cost of the examination. The Utah court has incidentally considered this matter already. Hence in the case of *Utah Farm Bureau Insurance Co. v. State Tax Commission*, 9 Utah 2d 421, 347 P.2d 179 (1959), the court held that the entire examination fee paid during the time that the Utah Farm Bureau Insurance Company operated as a stock company was deductible. The court said in that case that "*The statute permits stock companies to deduct the full amount of such examination costs from their tax liability. . . .*" (Emphasis added.) (9 Utah 2d at 427).

In *Equitable Life & Casualty Ins. Co. v. State Tax Commission*, 122 Utah 293, 249 P.2d 955 (1952) the court held that the cost of an insurance examination is deductible only in the year in which such is paid. The only limitation suggested by the court in that case, after a careful review of legislative history, is that such costs

cannot be "carried over" into subsequent years. Implicit in these decisions is the apparently unquestioned assumption that examination costs can be fully deducted in the year paid. While the court in these cases did not pass upon the exact question we have here presented, it is interesting to note no qualification in the language adopted by our court and no indication of any recognition of a basis for proration.

POINT III

THE PRORATION "FORMULA" ADOPTED BY THE TAX COMMISSION HAS NO BASIS.

It is submitted that there is no basis in law or reason for the formula adopted by the Tax Commission. It is a stipulated fact that the scope and comprehensiveness of these examinations is unrelated to the amount of premiums paid in Utah as compared with premiums paid in other states. (Finding 5 (e), R. 28). Yet, that is the basis for the Tax Commission's disallowance of a portion of the deduction. (See "Preliminary Statement," R. 4, letter dated February 24, 1960, R. 5, "Preliminary Statement," R. 7-10, and Tax Commission Finding of Fact 4, R. 27.)

Since there is no relationship between the comprehensiveness of these examinations and premiums paid in any particular state, *it follows that the cost of the examination can have no direct relationship to premiums paid or business done in any particular state.*

Apart from the logical argument just asserted against proration of the deduction, it is submitted that the statute itself admits of no such proration. There is

an absence of any indicated legislative policy or standards for such alleged proration in the statute. It is horn-book law that the legislature may not delegate legislative functions to an administrative agency, and a fortiori, it is fundamental that an administrative agency may not presume to assert legislative prerogatives *in the absence* of a purported enactment. But such is the case as to the purported "formula" adopted by the Tax Commission. There is no suggestion in the statute in question (31-14-4, U.C.A. 1953) that the permitted deduction may be prorated. Contrast this with such contrary enactments as the Utah franchise tax act wherein the legislature did contemplate a basis for proration and set forth a guidepost and standard to guide the commission in establishing such a rule or regulation. (See U.C.A. 1953, 59-13-20) The purported "formula" or rule of the Tax Commission should be struck down as unauthorized by statute. This is true because administrative rules and regulations may be promulgated only if authorized by legislative policy or standards contained in the statute. See 42 Am. Jur., Public Administration Law, §§ 43, 44. Such is not the case herein, and the purported action of the Tax Commission comes within the rule of *State v. Goss*, 79 Utah SS9, 11 P.2d 340 (1932) wherein the court held that a rule promulgated by the State Board of Health respecting receptacles to be used in serving the public with beverages was beyond the power of the State Board of Health.

In addition to the foregoing, the "formula" adopted by the Tax Commission, as applied in this case, is fallacious. First, charges in excess of the \$4,230.92, which

the Tax Commission has allowed, were directly and personally undertaken and incurred by the Utah insurance commissioner. The expenses of the "examiner in charge" in the amount of \$3,932.20 and the expenses of the actuary in the amount of \$3,892.13, making a total of \$6,824.33, were *personally* authorized by the Utah commissioner without so much as a contact with the NAIC or any other organization. (See Finding 9, R. 30). (In making this statement we do not retreat from the basic position herein that *all* costs were incurred by the Utah commissioner in that all examiners were designated and accepted by the Utah commissioner and their bills for services were approved and authorized by the Utah commissioner.) In any event, it is clear that charges directly authorized by the Utah commissioner exceed the rigid formula allocation which the Tax Commission has allowed. Can there be any reasonable doubt that these charges were directly "required" when our insurance commissioner personally appointed these men to examine the Surety Life Insurance Company and to be directly responsible to him?

The other anomaly respecting the formula which has been used by the Tax Commission is that the formula itself abandons the theory of the case of the Tax Commission. That theory is that the "*Utah portion*" of the examination must be *only a part* of the "*association*" or "*zone*" examination. If such were true, the cost of the examination should bear a direct relationship to premiums received *within the states represented by the zones*. As applied to Surety, however, the formula sets forth a

relationship between premiums paid in Utah and premiums paid in *all states* wherein Surety Life did business in 1959, *including states not within the zones represented in the "association" examination*. Hence, in the formula as set forth by the Tax Commission, \$70,843.28 of business done in South Dakota (not within either zones V or VI), and \$113,146.24 of business done in other states not within the zones was included as the basis for the proration. The essential point in this connection is that these states and areas were not, under the Tax Commission's own theory, "represented" in the examination since they were not within the zones specified as participating in the examination. Yet, inclusion by the Tax Commission of these premiums within the rigid "formula" serves to dilute the allowable deduction. Such inclusion is inconsistent with the zone-"association" theory of deduction as espoused by the Tax Commission.

To demonstrate the basic fallacy of the formula and its inapplicability as a general proposition, postulate these situations relative to an examination costing \$15,000.00. It shall be assumed relative to the following hypothetical examples that the same announced formula of premiums paid in Utah relative to premiums paid in all states is applicable:

1. Company A

Does 20 percent business in Utah and the Utah commissioner authorizes employment of examiners in Utah, resulting in 50 per cent (\$7,500.00) direct Utah costs. Result: Allow 20 per cent deduction, or \$3,000.00.

2. Company B

Does 80 per cent business in Utah and the Utah commissioner authorizes employment of examiners in Utah, resulting in 50 per cent (\$7,500.00) direct Utah costs. Result: Allow 80 per cent deduction, or \$12,000.00.

3. Company C

Does 5 per cent business in Utah and the Utah commissioner authorizes employment of examiners in Utah, resulting in 50 per cent (\$7,500.00) direct Utah costs. Result: Allow 5 per cent deduction, or \$750.00.

In the examples above postulated it will be noted that the only factor of significance is the relationship between premiums paid in Utah to premiums paid in all other states. The result is that the proportionate allowance of deduction is completely unrelated to expenses directly authorized by the Utah commissioner. Now let us inject the "zone"-type feature into the above hypothetical examples, and as to each let us assume that the areas participating in the examination are from zones and states in which the company does 50 per cent of its business in relationship to the entire amount of business that the company does throughout the United States. Under this state of facts, still adhering to the formula as set forth by the Commission, the results would nevertheless

be identical as set forth above but with the anomalous result that the allowed deduction would bear no relationship to the states and areas "represented" within the examination.

Translating the above hypothetical examples into the facts and circumstances of this case, we have in less exaggerated form the two principles present: first, that expenses and costs directly authorized by the Utah insurance commissioner exceed the amount of deduction that is allowable under the formula; second, that the amount of business done within the entire United States was more than the amount of business done within the zones represented by the examination. The result is that the formula as adopted by the Tax Commission bears no relationship to the zone theory of the Tax Commission, and even more important, it bears no relationship whatsoever *to the responsibility of the Utah commissioner for the conduct of the examination.*

CONCLUSION

The Company requests that the decision of the State Tax Commission of Utah rendered September 29, 1961, be nulled, vacated and set aside, and that the said Commission be ordered to render a new decision allowing to the Company the full deduction of examination costs as originally computed on its Insurance Premium Tax Return for the calendar year 1959. It is submitted that the

Tax Commission erred as a matter of law in its interpretation of Utah statutes and that its administrative ruling is without sanction of law. For these reasons the Company requests the relief prayed for by this Honorable Court.

Respectfully submitted,

J. THOMAS GREENE
MARR, WILKINS & CANNON
Attorneys for Appellant
920 Continental Bank Building
Salt Lake City, Utah